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No. _____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

TEXAS EASTERN TRANSMISSION CORPORATION,
Petitioner,

v.

FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK, *et al.*,
Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

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PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the placement of a private corporation's stock in trust for the benefit of a foreign government as part of an insolvency proceeding is sufficient to convert the corporation into a "foreign state" for purposes of federal jurisdiction under the Foreign Sovereign Immunities Act, 28 U.S.C. § 1603(a).

2. Whether, in a case in which federal jurisdiction is premised solely on diversity of citizenship, 28 U.S.C. § 1332(a), a court's assertion of federal jurisdiction over state-law counterclaims against nondiverse parties not originally in the case is consistent with the principles of pendent-party jurisdiction articulated in *Finley* v. *United States*, 490 U.S. 545 (1989).

PARTIES TO THE PROCEEDING

The parties to the proceeding in the court below were petitioner Texas Eastern Transmission Corporation[*/] and the following respondents: Fidelity and Casualty Insurance Company of New York; Associated Electric & Gas Insurance Services, Ltd.; Aetna Casualty and Surety Company; American Home Assurance Company, a/k/a American Home Insurance Company; Boston Old Colony Insurance Company; Cigna Insurance Company; Continental Casualty Company; Employers Mutual Company; First State Insurance Company; Highlands Insurance Company; The Home Insurance Company; The Insurance Company Of North America; Insurance Company Of The State Of Pennsylvania; International Insurance Company; Lexington Insurance Company; Midland Insurance Company; National Surety Corporation; Prudential Reinsurance Company; Ranger Insurance Company; Republic Insurance Company; Stonewall Insurance Company; United States Fire Insurance Company; Certain Underwriters at Lloyd's, London and Certain London Market Insurance Companies.

[*/] In accordance with Supreme Court Rule 29.1, the parent companies and nonwholly owned subsidiaries of petitioner Texas Eastern Transmission Corporation are listed at App. 340-41.

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v.

FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK, *et al.*,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Texas Eastern Transmission Corporation respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit in this case.

OPINIONS BELOW

The opinions below of the court of appeals (App. 6-68) are reported at 15 F.3d 1230 (3d Cir. 1994) and 15 F.3d 1249 (3d Cir. 1994). The opinions of the district court (App. 106-312) are unreported.

JURISDICTION

The court of appeals denied a petition for rehearing on February 3, 1994. (App. 4-5.) On April 21, 1994, Justice Souter extended the time for filing a petition for a writ of certiorari to and including July 1, 1994. (App. 1.) The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

28 U.S.C. § 1332(a) provides:

> (a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $50,000, exclusive of interest and costs, and is between —
>
> (1) citizens of different States;
> (2) citizens of a State and citizens or subjects of a foreign state;
> (3) citizens of different States and in which citizens or subjects of a foreign state are additional parties; and
> (4) a foreign state, defined in section 1603(a) of this title, as plaintiff and citizens of a State or of different States.
>
> For the purposes of this section, section 1335, and section 1441, an alien admitted to the United States for permanent residence shall be deemed a citizen of the State in which such alien is domiciled.

28 U.S.C § 1603(a) - (b) provides:

For purposes of this chapter —

(a) A "foreign state", except as used in section 1608 of this title, includes a political subdivision of a foreign state or an agency or instrumentality of a foreign state as defined in subsection (b).

(b) An "agency or instrumentality of a foreign state" means any entity —

(1) which is a separate legal person, corporate or otherwise, and
(2) which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof, and
(3) which is neither a citizen of a State of the United States as defined in section 1332(c) and (d) of this title, nor created under the laws of any third country.

STATEMENT OF THE CASE

1. Petitioner Texas Eastern Transmission Corporation ("TETCO") owns and operates several natural gas pipelines in a system that extends approximately 10,000 miles from the Gulf Coast of Texas and Louisiana to the New York metropolitan area. TETCO's pipelines use turbine-driven compressors to propel the gas. In 1958, TETCO began using a liquid containing polychlorinated biphenyls ("PCBs") as a lubricant in certain of the compressors. These lubricants eventually mixed with other liquids in the

pipeline system. Over several years, TETCO removed these liquids from the pipeline system and, consistent with standard industry practice, discharged some of these liquids into unlined earthen pits. The liquids in these pits subsequently contaminated the property of TETCO and third parties through overflow and other discharges. In addition, the liquids escaped into the environment from the pipeline system through leaks, spills, and other unintentional discharges.

During the 1980s, TETCO began negotiating with federal and state agencies concerning its statutory responsibilities with respect to the PCB contamination caused by the pipeline liquids. In June 1988, TETCO entered into a consent agreement with the EPA that obligated TETCO to remediate property contaminated by PCBs. TETCO also entered into similar consent decrees with several state environmental agencies. In addition to these cleanup obligations, TETCO incurred liabilities to private third parties for property damage and personal injuries.

2. Respondents are twenty-three insurance companies ("the insurers") that sold approximately 110 policies of primary and excess comprehensive general liability ("CGL") insurance to TETCO between 1958 and 1987. Although the language of the insuring agreement in these policies varies, most of the policies essentially provide that the insurers will indemnify TETCO for "all sums which the insured shall become legally obligated to pay as damages because of bodily injury or property damage caused by an occurrence during the policy period." The policies also require TETCO to provide notice of a claim under the policies "as soon as practicable."

In a letter dated August 19, 1987, TETCO officially

notified the insurers of a claim for coverage under its CGL policies for the sums it was obligated to pay as a result of the PCB contamination from its pipeline system. This insurance claim resulted in the three lawsuits, later consolidated, that are the subject of this petition:

a. *F&C* Case. On December 11, 1987, respondent Fidelity & Casualty Company of New York ("Fidelity" or "F&C"), TETCO's primary CGL carrier throughout the relevant period, sued TETCO in the United States District Court for the Northern District of Texas. Federal jurisdiction was premised on diversity of citizenship. F&C sought a declaratory judgment concerning its duty to defend or indemnify TETCO under the CGL policies for sums paid by TETCO as a result of claims by the EPA, state agencies, and private parties.

b. *AEGIS* Case. On March 11, 1988, respondents Associated Electric & Gas Insurance Services Limited ("AEGIS") and National Surety Corporation ("National Surety") sued TETCO and the remaining insurers in the United States District Court for the Eastern District of Pennsylvania. The *AEGIS* complaint sought a declaratory judgment concerning the plaintiffs' rights and duties under the CGL policies.

Diversity jurisdiction was not available in the *AEGIS* case, because AEGIS shared citizenship with many of the insurer-defendants. Instead, AEGIS and National Surety maintained that federal jurisdiction was proper under the Foreign Sovereign Immunities Act ("FSIA"), 28 U.S.C. §§ 1330(a), 1603(a), 1605(a)(2). FSIA jurisdiction was premised on the contention that one of the insurer-defendants, the Insurance Corporation of Ireland ("ICI"), was a "foreign state" within the meaning of the FSIA.

ICI's alleged foreign sovereign status was based on the following facts, which are not in dispute. ICI was incorporated in the Republic of Ireland as a private company in 1935. As a private corporation, it subscribed to some of the insurance contracts at issue here between 1978 and 1985. By 1985, it became overextended and lacked sufficient reserves to cover its liabilities. Accordingly, pursuant to an order by Ireland's High Court, ICI was placed under "administration," a procedure involving a potentially indefinite period of court protection that is similar to Chapter 11 protection under United States bankruptcy law. As part of this procedure, virtually all of ICI's stock was acquired by Sealuchais Archais Teoranta ("SAT"), a private limited liability company. Since March 18, 1985, the shareholders and directors of SAT have been two individuals who have held their shares in SAT in trust for Ireland's Minister of Industry and Commerce. Neither the Minister nor the Irish government holds legal title to any stock in either ICI or SAT.

c. *Texas Eastern* Case. On March 21, 1988, TETCO filed a comprehensive action in Texas state court against all of its insurers seeking a declaratory judgment and damages under Texas law.[1/] On June 3, 1988, the insurers removed the entire case to the United States District Court for the Southern District of Texas. Removal jurisdiction was asserted under the FSIA solely on the basis of the alleged foreign sovereign status of a single insurer, ICI.

3. On May 31, 1988, the Judicial Panel on

[1/] Texas Eastern had previously filed an essentially identical action against the insurers in New Jersey state court on December 21, 1987. That suit was subsequently dismissed on March 17, 1988, on the ground of *forum non conveniens*.

Multidistrict Litigation transferred the *F&C* case pursuant to 28 U.S.C. § 1407 to the Eastern District of Pennsylvania and consolidated it there with the *AEGIS* case for pretrial proceedings. In July 1988, the United States District Court for the Southern District of Texas transferred the *Texas Eastern* action to the Eastern District of Pennsylvania prior to ruling on TETCO's motion to remand the case to state court. *Texas Eastern* was then consolidated with the other two cases.

Following consolidation of the three cases in the Eastern District of Pennsylvania, TETCO moved to remand the *Texas Eastern* action to Texas state court and to dismiss or stay the *AEGIS* action. In support of these motions, Texas Eastern argued that the court lacked subject-matter jurisdiction because ICI was not a "foreign state" within the meaning of the FSIA. Assuming in the alternative that ICI was a foreign state, TETCO maintained that the service-of-suit clause in the CGL policies constituted a waiver of ICI's right to remove the *Texas Eastern* case.[2/] TETCO also argued that the *AEGIS* case should be dismissed because, after a necessary realignment of the parties based on their true interests, the suit was not "against a foreign state" as is required for jurisdiction under the FSIA, 28 U.S.C.

2/ The service-of-suit clause provides:

> It is agreed that in the event of the failure of the Underwriters hereon [*i.e.*, ICI] to pay any amount claimed to be due hereunder, Underwriters hereon at the request of the Insured (or Reinsured) will submit to the jurisdiction of any Court of competent jurisdiction within the United States and will comply with all requirements necessary to give such Court jurisdiction and all matters arising hereunder shall be determined in accordance with the law and practice of such court.

§ 1330(a). Although TETCO did not challenge subject-matter jurisdiction in the *F&C* case (because at that time the *F&C* case involved only the diverse parties TETCO and F&C), it did move to stay or dismiss the *F&C* case in deference to the more comprehensive *Texas Eastern* case.

At a hearing on September 15, 1988, the district court rejected TETCO's jurisdictional arguments. (App. 282-312.) The court held that, once the shares of ICI's holding company, SAT, were placed in trust for the benefit of the Irish Minster of Industry and Commerce, ICI automatically became a "foreign state" under the FSIA. (App. 295-98.) In addition, the court held that the parties in the *AEGIS* case were properly aligned for purposes of federal jurisdiction under the FSIA (App. 293-95), and that ICI had not waived its right to remove the *Texas Eastern* case to federal court, (App. 302-04). Finally, the court rejected TETCO's motion to stay or dismiss the *F&C* case. (App. 306.)

After the district court rejected TETCO's jurisdictional arguments, TETCO filed an answer in the *F&C* case and asserted counterclaims against the single plaintiff, F&C. In addition, as a precautionary measure, TETCO joined its twenty-two excess insurers (six of which shared the same citizenship as TETCO) "as co-defendants in the counterclaims" (App. 13), pursuant to Fed. R. Civ P. 13(h).

Following limited discovery, the parties filed cross-motions for summary judgment. The district court granted the insurers' motion, holding that TETCO was barred from recovering against the insurers because it had failed to provide them with timely notice of the matters for which it would seek coverage. (App. 106-281.)

TETCO appealed the district court's rulings on both the

jurisdictional issues and the merits. On May 28, 1993, the court of appeals affirmed the district court in an unpublished opinion. (App. 76-103.) The court held that ICI "qualifies as a 'foreign state' because the Republic of Ireland owns 100% of its stock and has assumed its obligations." (App. 81.) The court further rejected TETCO's arguments that ICI had waived its right to remove the *Texas Eastern* case and that ICI should be realigned as a party plaintiff in the *AEGIS* case. (App. 81-82 & n.1.) Finally, the court affirmed the district court's conclusions concerning late notice. (App. 83-92.) Judge Alito filed a dissenting opinion. (App. 93-103.)

On June 10, 1993, TETCO filed a petition for panel rehearing and suggestion for rehearing in banc, arguing that the panel opinion's jurisdictional rulings conflicted with precedents from the Third Circuit and other Circuits. Over the next several months, both TETCO and the insurers filed additional documents with the court of appeals concerning, *inter alia*, whether the excess insurers were properly joined in the *F&C* case pursuant to TETCO's counterclaims against F&C, and, if so, whether the court possessed ancillary or pendent jurisdiction over the nondiverse excess insurers. On August 18, 1993, the original panel issued an order granting TETCO's request for rehearing and asking the parties to address three questions: "1) [T]he structure and purpose of 28 U.S.C. § 1330; 2) [W]hat claims, if any, have been asserted by AEGIS against ICI; [and] 3) [W]hether the presence of all parties destroys supplemental jurisdiction in the *F&C* case." (App. 74.)

After supplemental briefing and reargument, the original panel issued an opinion for publication reaching the same jurisdictional conclusions that it had reached in its

earlier decision. (App. 6-48.)[3/] The court once again rejected TETCO's argument that ICI was not a "foreign state" within the meaning of the FSIA:

> We uphold the district court's finding that ICI is a "foreign state" within the meaning of 28 U.S.C. § 1603(a). The district court has determined that ICI is an "agency or instrumentality of a foreign state" in that it is a separate legal person, a majority of its shares are owned by a foreign state, the Republic of Ireland, and it is neither a citizen of a state of the United States, nor created under the laws of a third country. These findings are not clearly erroneous.

(App. 23 n.8.) The court also again rejected TETCO's waiver and realignment arguments, albeit for reasons somewhat different than those expressed in its earlier decision. (App. 21-36.)

In addition, the court of appeals rejected TETCO's arguments regarding the scope of jurisdiction in the *F&C* case. The court first held that the excess insurers were properly joined to the counterclaims TETCO asserted against F&C. (App. 16-17.) The court then rejected TETCO's contention that the district court's exercise of subject-matter jurisdiction over the counterclaims against the nondiverse excess insurers was a form of pendent-party jurisdiction precluded by the Supreme Court in *Finley* v. *United States*, 490 U.S. 545 (1989). Relying on this Court's decision in *Owen Equipment & Erection Co.* v.

[3/] The Third Circuit issued two opinions, one discussing jurisdiction (App. 6-49) and the other discussing the merits (App. 50-69).

Kroger, 437 U.S. 365, 376 (1978), and a pre-*Finley* Third Circuit decision, the court distinguished (and thus refused to apply) *Finley* on the "subtle" ground that claims against the nondiverse parties in the *F&C* case were asserted by a defendant rather than a plaintiff. (App. 17-19.) The court concluded that the "additional non-diverse counterclaim defendants do not destroy diversity jurisdiction in the *F&C* action because there is complete diversity of citizenship between the original named parties." (App. 21.)

Judge Alito again dissented. "Assuming that ICI falls within 28 U.S.C. § 1603's definition of a 'foreign state,'" Judge Alito argued that the majority erred in concluding that it had jurisdiction in the *Texas Eastern* and *AEGIS* cases under the FSIA. (App. 38-45.) Judge Alito declined to consider TETCO's arguments concerning joinder and jurisdiction in the *F&C* case. Instead, he would have vacated the *Texas Eastern* and *AEGIS* cases and remanded the *F&C* case to the district court for an initial determination of whether the excess insurers were properly joined and "whether, despite *Finley*, the district court could exercise subject matter jurisdiction over the counterclaims." (App. 45-48.)

Following this decision, TETCO filed a petition for rehearing, which was denied on February 3, 1994. (App. 4-5.)[4/]

[4/] The district court recently held a status conference concerning matters collateral to the three cases and granted a stay of all such matters pending resolution of this certiorari petition. (App. 2-3.)

REASONS FOR GRANTING THE PETITION

This petition presents two important issues of federal jurisdiction, both of which implicate conflicts of authority in the lower courts.

I. THERE IS A CONFLICT IN THE COURTS REGARDING WHETHER THE PLACEMENT OF A PRIVATE CORPORATION'S STOCK IN TRUST FOR THE BENEFIT OF A FOREIGN GOVERNMENT AS PART OF AN INSOLVENCY PROCEEDING IS SUFFICIENT TO CONVERT THE CORPORATION INTO A "FOREIGN STATE" FOR PURPOSES OF FEDERAL JURISDICTION UNDER THE FOREIGN SOVEREIGN IMMUNITIES ACT.

The FSIA defines a "foreign state" to include "a political subdivision of a foreign state or an agency or instrumentality of a foreign state." 28 U.S.C. § 1603(a). "Agency or instrumentality" is in turn defined in relevant part as "any entity . . . which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof." 28 U.S.C. § 1603(b)(2).

In both the district court and the court of appeals, TETCO argued that ICI is not a "foreign state" under the FSIA because (a) the Irish government has at most an indirect ownership interest in ICI's shares, (b) the government does not exercise control over ICI's operations, and (c) ICI does not serve a public purpose. The lower courts, however, concluded that the "administration" procedure described above, whereby the stock of ICI's holding company, SAT, was placed in trust for the benefit

of the Irish Minister for Industry and Commerce, was sufficient to convert ICI into a foreign state.

The lower courts' determination that ICI is a "foreign state" under the FSIA directly conflicts with decisions by district courts in three other Circuits, which have held that ICI is *not* a "foreign state" under the FSIA. *See Aluminum Co. of America* v. *Admiral Ins. Co.*, No. C93-32C (W.D. Wash. Apr. 9, 1993) (App. 313-15); *Murphy Oil USA, Inc.* v. *United States Fidelity & Guar. Co.*, No. 91-1157, 1992 WL 465701 (W.D. Ark. Dec. 21, 1992) (App. 316-31); *Mobil Corp.* v. *Abeille Gen. Ins. Co.*, No. H-89-3877, 1990 WL 504828 (S.D. Tex. Nov. 6, 1990) (App. 332-39), *appeal dismissed*, 984 F.2d 664 (5th Cir. 1993). Another court has specifically noted the "conflicting opinions" on this issue. *Tennessee Gas Pipeline Co.* v. *Continental Casualty Co.*, 814 F. Supp. 1302, 1306 n.6 (M.D. La. 1993).

This division is the functional equivalent of a conflict in the Circuits, because the three district court decisions holding that ICI is not a foreign state (and therefore remanding the cases back to state court) were not appealable. Except in certain civil rights cases, "[a]n order remanding a case to the State court from which it was removed is not reviewable on appeal or otherwise." 28 U.S.C. § 1447(d). Section 1447(d) has specifically been applied to bar appellate review in a case holding that ICI is not a foreign state. *See Mobil Corp.* v. *Abeille General Ins. Co.*, 984 F.2d 664, 666 (5th Cir. 1993).

There could not be a clearer conflict of authority: different courts have reached opposite conclusions regarding the "foreign state" status of the *very same entity*, ICI. They did so despite their application of the same statute, 28 U.S.C. § 1603, to the same facts concerning the Irish

government's relationship with ICI.

In *Mobil*, the court emphasized that "[n]either the Minister for Industry and Commerce nor the Irish government holds legal title to any stock in either ICI or SAT." (App. 334.) The court went on to hold that, "[e]ven if the Irish government has an ownership interest in ICI *this courts jurisdiction is not automatic*." (*Id.* (emphasis added).) Rather, the court looked to two "'more precise indices'" of an entity's status: "'the degree to which the entity discharges a governmental function, and the extent of state control over the entities operations.'" *(Id.)* (quoting *Edlow International Co.* v. *Nuklearna Elektrarna KRSKO*, 441 F. Supp. 827, 832 (D.D.C. 1977)). Those "more precise indices" are precisely the factors that the lower courts in this case refused to consider.[5/]

This issue of the "foreign state" status of foreign companies that become insolvent and have their shares placed in trust is of widespread significance, especially in the insurance industry. With increasing environmental and other liabilities, many foreign insurers are now facing potential insolvency. This is particularly true in the London insurance market, of which ICI is a part, where over a dozen insurers have become insolvent in the last several

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[5/] In *Murphy Oil*, the court reviewed the *Mobil* decision at length and found its reasoning and conclusions "persuasive." (App. 330.) In *ALCOA*, the court reviewed both *Mobil* and *Murphy Oil*, found them "persuasive," and, indeed, believed that the issue was sufficiently clear that ICI should be barred from further claiming that it is a "foreign state." (App. 315.)

years.[6] The use of trust and similar arrangements, whereby the shares of private corporations are held for the benefit of foreign governments, is thus likely to increase substantially in the future.

The lower courts' rulings — which allow private companies to become "foreign states" simply by virtue of trust arrangements established as part of insolvency proceedings — could therefore lead to massive abuse of the procedural and substantive rights granted under the FSIA. It will mean that, as in this case, essentially private insurance companies like ICI will be able to:

- defeat otherwise-valid contractual choice-of-forum clauses;[7]
- use artificial pleading arrangements to create federal jurisdiction;[8]

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[6] Richard Lapper, *Crisis Reaches Small Insurance Companies; Problems in Lloyd's Market Have Spread,* Financial Times, Jan. 14, 1993, at 21.

[7] At the time that ICI agreed to the service-of-suit clause in the insurance policies at issue in this case, it was indisputably a private corporation. Courts (including the Third Circuit) normally interpret such clauses to constitute a waiver of the right to remove a case to federal court. *See, e.g., Foster* v. *Chesapeake Ins. Co.*, 933 F.2d 1207 (3d Cir.), *cert. denied,* 112 S.Ct. 302 (1991). Nevertheless, the court below held that ICI's post-contractual transformation into a "foreign state" rendered ICI's waiver unenforceable. (App. 35-36. *But see* App. 42 (Alito, J., dissenting).)

[8] Faced with a lack of diversity jurisdiction, the plaintiff-insurers in the *AEGIS* case named ICI — another insurer with identical interests — as a party defendant in a declaratory judgment suit so that the case would appear to be "against a foreign state" for purposes of obtaining FSIA jurisdiction.

- manipulate removal, transfer, and consolidation provisions so that a federal court unfamiliar with the state law at issue decides the case;[9] and

- bring other similarly-interested companies with no claim to "foreign state" status along with them into federal court.[10]

In another case involving the Insurance Corporation of Ireland, this Court reiterated the fundamental principle that federal courts are courts of limited jurisdiction and that the boundaries of their subject-matter jurisdiction must be strictly maintained. *Insurance Corp. of Ireland* v. *Compagnie des Bauxites de Guinee*, 456 U.S. 694, 701-02 (1982). This Court should grant review to resolve the conflict in the courts regarding ICI's status and to enforce the proper limits of federal subject-matter jurisdiction.

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[9] The district court acknowledged at oral argument on summary judgment that it "ha[d]n't the faintest what Texas law is" (Hearing Tr. Jan. 13, 1992, at 31), and its opinion noted "the difficulty and irony of a federal district court judge sitting in Pennsylvania predicting what the Supreme Court of Texas would do if faced with particular questions, given that two of the three cases consolidated in this action originated in Texas and concern activities which primarily occurred there." (App. 122 n.12.) Judge Alito's dissent reiterated the oddity of the federal courts in the Third Circuit deciding "difficult, unsettled, and controversial questions of Texas insurance law" based on "erroneous jurisdictional premises." (App. 38 (Alito, J., dissenting).)

[10] The twenty-three respondent-insurers were present in federal court in the *Texas Eastern* and *AEGIS* lawsuits only because ICI had subscribed, as a foreign private corporation, to a few of the many policies of excess coverage obtained by TETCO through one of TETCO's many insurers, Lloyd's of London. ICI was liable for at most $8 million of the billions of dollars of insurance coverage potentially at issue.

II. THE ASSERTION BY THE COURT OF APPEALS OF FEDERAL JURISDICTION OVER TETCO'S CLAIMS AGAINST THE NONDIVERSE EXCESS INSURERS IS INCONSISTENT WITH THIS COURT'S DECISION IN *FINLEY* v. *UNITED STATES*, AND CONFLICTS WITH A DECISION IN THE FIFTH CIRCUIT.

TETCO argued before the court of appeals that the assertion of federal jurisdiction in the *F&C* case over the counterclaims filed against the nondiverse excess insurers under Rule 13(h) was prohibited by this Court's decision in *Finley* v. *United States*, 490 U.S. 545 (1989). The court of appeals' rejection of this argument is inconsistent with *Finley* and directly conflicts with the Fifth Circuit's decision in *Birmingham Fire Ins Co. of Pa.* v. *Winegardner and Hammons, Inc.*, 714 F.2d 548 (5th Cir. 1983).

In *Finley*, this Court considered whether a party suing the federal government under the Federal Tort Claims Act ("FTCA"), 28 U.S.C. § 1346(b), could also assert against a private party a claim for which there was no independent basis of federal jurisdiction. The Court stated that this issue involved the validity of "pendent party jurisdiction," which the Court defined broadly as "jurisdiction over parties not named in any claim that is independently cognizable by the federal court." 490 U.S. at 549 (emphasis omitted). Relying on three prior Supreme Court decisions,[11/] the Court held that "a grant of jurisdiction over claims involving particular parties does not itself confer jurisdiction over additional claims by or against different parties." *Id.*

11/ *Owen Equip. & Erection Co.* v. *Kroger*, 437 U.S. 365 (1978); *Aldinger* v. *Howard*, 427 U.S. 1 (1976); *Zahn* v. *International Paper Co.*, 414 U.S. 291 (1973).

at 556. Because the FTCA did not expressly authorize federal jurisdiction over the additional claim brought against the additional party, the Court dismissed the claim. *Id.*

The claims against the nondiverse excess insurers in this case, like the claims against the pendent party in *Finley*, are "added claims involv[ing] added parties over whom no independent basis of jurisdiction exists." *Id.* at 551. *Finley*'s prohibition of federal jurisdiction over claims against such pendent parties applies when the primary claim is brought under the diversity statute, for as the *Finley* Court made clear, that statute authorizes jurisdiction over suits between "citizens of different States *and no one else*." *Id.* at 552 (emphasis added). Accordingly, *Finley* prohibits the assertion of federal jurisdiction over the claims against the nondiverse excess insurers.

Relying on a misinterpretation of dicta in this Court's decision in *Owen Equipment & Erection Co.* v. *Kroger*, 437 U.S. 365 (1978), and on a pre-*Finley* Third Circuit decision, the court of appeals attempted to distinguish *Finley* on the "subtle" ground that the pendent-party claims here were brought by a defendant "haled into court against his will" rather than by a plaintiff who initiated the lawsuit. *Finley*, however, addressed and rejected essentially the same argument. After noting that, "unlike in *Kroger*, the party seeking to bring the added claims had little choice but to be in federal rather than state court, since the FTCA permits the Federal Government to be sued only there," the *Finley* Court held that "*that [difference] alone is not enough*" to permit pendent-party jurisdiction. *Finley, 490 U.S.* at 552 (citation omitted) (emphasis added). In addition, in response to Justice Stevens' dissent, the *Finley* Court made clear that its elimination of pendent-party jurisdiction extended to third-party claims under Fed. R. Civ. P. 14(a), which include claims made by defendants haled into court

against their will. *Id.* at 553 n.6.

The decision below thus flies in the face of *Finley*. It also directly conflicts with the Fifth Circuit's decision in *Birmingham Fire Ins Co.* v. *Winegardner and Hammons, Inc.*, 714 F.2d 548 (5th Cir. 1983). There, a Texas corporation owned a hotel that was damaged by a hurricane. One of its insurers, a Pennsylvania corporation, initiated a diversity action seeking a declaratory judgment under state law with respect to its liability. The defendant hotel asserted a state-law counterclaim against that insurance company and a second, nondiverse Texas insurer. Relying on *Aldinger* and *Kroger*, the Fifth Circuit held that it lacked jurisdiction over the counterclaim against the nondiverse insurer. *Id.* at 552-54.

Birmingham Fire is in direct conflict with the decision below. In both cases, a plaintiff-insurer brought a state-law coverage suit under the diversity statute, and the defendant-insured asserted counterclaims against the original plaintiff and additional nondiverse insurers not previously in the case. Although both courts relied primarily on this Court's decision in *Kroger*, they reached antithetical conclusions: *Birmingham Fire* rejected the assertion of jurisdiction over the pendent parties, while the court below permitted it. In addition, the Fifth Circuit expressly rejected the Third Circuit's rationale based on *Kroger* for asserting federal jurisdiction:

> [*Kroger*] is analytically indistinguishable from the case now before us. Although there it was the plaintiff which initiated all the litigation, whereas in this case Holiday Inn is a cross-plaintiff and did not originate the litigation but rather was forced to answer BFI's motion for declaratory judgment, that distinction is not

> significant. And it is certainly not enough to overcome the general diversity requirement.

Id. at 553.

The conflict with *Finley* and *Birmingham Fire* implicates important issues of federal-state relations. *Finley*'s strict rule of construction for federal jurisdiction statutes derives from the constitutional concern of protecting state prerogatives. 490 U.S. at 552-53; *see also id.* at 577 (Stevens, J., dissenting) (noting lack of federal interest in resolution of state law claim of pendent party when jurisdiction based on diversity of citizenship). As this Court has long made clear:

> The power reserved to the states under the Constitution to provide for the determination of controversies in their courts, may be restricted only by the action of Congress in conformity to the Judiciary Articles of the Constitution. Due regard for the rightful independence of state governments, which should actuate federal courts, requires that they scrupulously confine their own jurisdiction to the precise limits which the statute has defined.

Shamrock Oil & Gas Corp. v. *Sheets*, 313 U.S. 100, 108-09 (1941) (citations omitted). This federalism principle has special force in a case involving insurance law, which both Congress and this Court have recognized is the special province of the states. *See* McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015; *United States Dep't of the Treasury* v. *Fabe*, 113 S. Ct. 2202, 2207 (1993) (purpose of McCarran-Ferguson Act is "broadly to give support to existing and future state systems for regulating and taxing the business of insurance").

In sum, the exercise of jurisdiction over the counterclaims against the nondiverse excess insurers is inconsistent with *Finley* and *Birmingham Fire*, and impermissibly intrudes on state-law prerogatives.[12/]

[12/] Although the Court below correctly noted that the new supplemental jurisdiction statute, 28 U.S.C. § 1367 (Supp. 1992), does not apply in this case (App. 20), it nonetheless maintained that its assertion of jurisdiction over the counterclaims against the nondiverse excess insurers was consistent with the new statute (App. 20-21). This dictum is based on an erroneous reading of Section 1367 that further demonstrates the continuing significance of this case. Section 1367(b) reaffirmed *Finley*'s prohibition on pendent-party jurisdiction in diversity cases -- the point at issue here. Section 1367(b) provides that "the district courts shall *not* have supplemental jurisdiction . . . over claims by plaintiffs against persons made parties under Rule 14, 19, 20, or 24 of the Federal Rules of Civil Procedure." (Emphasis added.) TETCO asserted the counterclaims against the nondiverse excess insurers under Rule 13(h); the nondiverse excess insurers were therefore necessarily joined as counterclaim defendants pursuant to Rule 19 or 20. *See, e.g.*, Fed. R. Civ. P. 13(h) (authorizing counterclaims against "[p]ersons other than those made parties to the original action . . . *in accordance with the provisions of Rules 19 and 20*") (emphasis added). Thus, contrary to the dictum of the court below, Section 1367(b) would (if it applied) prohibit a court from exercising supplemental jurisdiction in a case like this one. *See, e.g., Mayatextil, S.A.* v. *Liztex U.S.A., Inc.*, No. 92 Civ. 4528, 1993 U.S. Dist. LEXIS 6527, at *7 (S.D.N.Y. May 18, 1993) ("Congress intended § 1367(b) to encompass Rule 13(h)."); *see also* Denis F. McLaughlin, *The Federal Supplemental Jurisdiction Statute — A Constitutional and Statutory Analysis*, 24 Ariz. St. L.J. 849, 940 n.471 (1992); Karen Nelson Moore, *The Supplemental Jurisdiction Statute: An Important But Controversial Supplement to Federal Jurisdiction*, 41 Emory L.J. 31, 56 n.82 (1992).

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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